06-54

Before the
Federal Communications Commission
Washington, D.C. 20554

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Federal Communications Commission
Office of Secretary

In the Matter of	)	
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Petition of the Verizon Local and	)	
Long Distance Telephone	)	
Companies for Forbearance Under	)	WC Docket No. _______
47 U.S.C. § 160(c) with Regard	)	
to Certain Dominant Carrier Regulations	)	
for In-Region, Interexchange Services	)	

PETITION OF VERIZON[1] FOR FORBEARANCE UNDER 47 U.S.C. § 160(c) WITH REGARD TO CERTAIN DOMINANT CARRIER REGULATIONS FOR IN-REGION, INTEREXCHANGE SERVICES

Verizon requests that the Commission forbear from certain aspects of dominant carrier regulation that would apply to Verizon's provision of in-region interexchange services after March 19, 2006, when the requirements of section 272 of the 1996 Telecommunications Act, 47 U.S.C. § 272, sunset with respect to the final three former Bell Atlantic states. The Commission also should forbear from certain limited regulations that apply to Verizon's provision of interexchange services in the former GTE region. The competitive landscape is very different from the last time the Commission looked at rules relating to provision of long distance service by affiliates of incumbent local exchange companies. Competition for all kinds of telephone services, including long distance services, is robust and vigorous. Where end users once bought local service from their local phone company and long distance service from one of a number of interexchange carriers, they now can choose among a variety of all distance services offered by a

[1] The Verizon companies participating in this filing ("Verizon") are the local exchange and long distance carriers affiliated with Verizon Communications Inc., which are identified in Attachment A.

wide range of intermodal providers. Cable companies, wireless carriers, and VoIP providers all offer services that compete with traditional wireline telephony and long distance services.

The Commission has long recognized that competition is the best form of "regulation." Consumers in all parts of the country will benefit from removing outmoded and artificial regulatory handicaps from the BOCs and incumbent independent LECs. Conversely, imposing tariffing, price cap, *Computer III*, and accounting regulations on BOCs' long distance services but not on other competitors, will harm the public interest. Similarly, imposing structural separation requirements on incumbent independent LECs that are not imposed on other competitors also harms the public interest. The Commission should, therefore, forbear from applying these rules to Verizon after the sunset of section 272 on March 19, 2006.

In particular, the Commission should forbear from section 203 of the Communications Act and from the following rules: (1) dominant carrier tariffing requirements set forth in Part 61 of the Commission's rules (e.g., 47 C.F.R. §§ 61.28, 61.32, 61.33, 61.38, 61.58, and 61.59) or any such rules that could be read to impose a tariff filing obligation on interstate interexchange or international services; and (2) price cap regulation on the retail interexchange offerings of Bell companies set forth in Part 61 of the Commission's rules (e.g., 47 C.F.R. §§ 61.41 – 61.49).[2] The Commission also should forbear from its accounting requirements to the extent that they require nonregulated treatment of interexchange services if Verizon decides to provide them through the ILECs on an integrated basis after the sunset of section 272; however, accounting for such services that continue to be provided through a separate affiliate should continue to be subject only to GAAP accounting requirements and not otherwise be subject to the Uniform

[2] Verizon's request to forbear from the tariffing and price regulation rules extends only to the provision and offering of long distance services and does not include access services.

System of Accounts set forth in Part 32 of the Commission's rules.[3] Verizon also requests forbearance from the *Computer III* requirements, including Comparably Efficient Interconnection ("CEI") and Open Network Architecture ("ONA") requirements for its interexchange services[4] and from certain Part 63 rules concerning the processes for acquiring lines, discontinuing services, assignments and transfers of control, and acquiring affiliations (47 C.F.R. §§ 63.12(b)(2), 63.19(b), 63.21(c), and 63.71(c) (second half of the subsection)). Finally, the Commission should forbear from its regulations that require incumbent independent (non-BOC) LECs providing in-region, interstate, interexchange or international services to provide such services through a separate affiliate that must maintain separate books of account and is prohibited from jointly owning transmission or switching facilities with the local exchange company (47 C.F.R.§ 64.1901-64.1903).

Verizon urgently needs this relief because section 272's structural and related requirements will sunset for Verizon in the last of its affected states on March 19, 2006. Verizon also includes the former GTE service territories. The former GTE companies are subject to structural separation requirements applicable to independent ILECs. 47 C.F.R. § 64.1903(a)(1),

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[3] Verizon requests forbearance from the applicability of *Implementation of the Telecommunications Act of 1996: Accounting Safeguards Under the Telecommunications Act of 1996*, 11 FCC Rcd 17539 (1996) to the extent this order would require integrated interLATA services offered after the sunset of section 272 to be treated as nonregulated for accounting purposes. The requested forbearance from the Commission's accounting rules would apply to all interLATA services provided by Verizon on an integrated basis if the Commission grants Verizon's petition.

[4] *See Amendment of Section 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry)*, 104 FCC 2d 958, ¶¶ 127-31 (1986); *Application of ONA and Nondiscrimination Safeguards to GTE Corporation*, 9 FCC Rcd 4922 (1994). CEI and ONA requirements do not apply to services provided by non-dominant interexchange carriers. *See Computer III Further Remand Proceedings: Bell Operating Company Provision of Enhanced Services; 1998 Biennial Regulatory Review -- Review of Computer III and ONA Safeguards and Requirements*, 14 FCC Rcd 4289 (1999) (noting that CEI and ONA requirements are not applicable to AT&T). Verizon's request here applies only to its interexchange services and not to intraLATA services provided by Verizon ILECs.

(2), (3). The structural separation requirements for the former GTE service areas will not sunset. Verizon does not offer a "GTE" long distance service separate from a "Bell Atlantic" long distance service. As a result, if the Commission continues to impose the independent ILEC structural separation requirements, it will condemn the company to operating its long distance business as a separate subsidiary even after the section 272 requirement to do so sunsets in the former Bell Atlantic service areas.

This petition is being submitted separately from its companion petition for limited waiver in compliance with section 1.53 of the Commission's rules. 47 C.F.R. § 1.53. A memorandum of points and authorities in support of this petition and the companion petition is attached hereto and incorporated herein by reference. As explained there, the present market situation plainly satisfies the forbearance criteria that the Commission has previously established.

The Commission has not just the power but the *duty*, under section 10 of the Communications Act, to forbear from enforcing Title II requirements if the Commission determines that: (1) the enforcement of such requirements is not necessary "to ensure that the charges, practices, classifications, or regulations" for the carrier or service in question "are just and reasonable and are not unjustly or unreasonably discriminatory"; (2) enforcement of such requirements is not necessary "for the protection of consumers"; and (3) forbearance is consistent with the public interest. 47 U.S.C. § 160.

Each of the three statutory requirements for forbearance from the specified regulations is satisfied. As for the first requirement, the Commission has held that "competition is the most effective means of ensuring that the charges, practices, classifications, and regulations with respect to [a telecommunications service] are just and reasonable, and not unjustly or unreasonably discriminatory."[5] Verizon's long distance services are not tariffed today. *Similarly, price cap regulation does not apply today to Verizon's long distance services; indeed,* no interexchange toll service is subject to price cap regulation. The CEI and ONA rules and the dominant carrier Part 63 rules also do not apply today to Verizon's long distance services. And the Commission has found that structural separation imposes additional costs and inefficiencies with no corresponding consumer benefit. Accordingly, enforcement of such requirements cannot be necessary "to ensure that the charges, practices, classifications, or regulations" for Verizon's long distance services "are just and reasonable and are not unjustly or unreasonably discriminatory."

Moreover, as discussed in the attached Memorandum, competition for all kinds of telephone services, including long distance services, has increased dramatically over the last decade. All providers of long distance services (whether the services are provided separately, as a bundle of local and long distance, or as "all distance" services) must compete in this changed marketplace.

The intermodal competitors are national in scope. For example, wireless providers such as Cingular, Sprint Nextel, and T-Mobile compete nationally. Similarly, any customer with a broadband connection – which, as explained in the attached Memorandum, is now available to more than 90 percent of U.S. households from a provider other than the incumbent LEC – can purchase VoIP services from many different providers including Vonage, Packet8, Lingo, and AT&T. The Commission has therefore found that "intermodal competitors, including facilities-based VoIP and mobile wireless providers, are likely to capture an increasing share of mass market local and long distance services." *Verizon / MCI Merger Order*, 20 FCC Rcd 18433

[5] *Petition of U S WEST Communications, Inc. for a Declaratory Ruling Regarding the Provision of National Directory Assistance*, 14 FCC Rcd 16252, ¶ 31 (1999).

¶ 105 (2005). Given the pressure of these competitors, there is no plausible claim that Verizon could charge unjust or unreasonable prices, or engage in unjust or unreasonable practices.

As for the second forbearance requirement, competition also ensures that the specified regulations are not "necessary for the protection of consumers." Instead, the opposite is true: consumers are best protected by allowing the marketplace to provide them with a robust choice of services from a variety of competing providers. Indeed, the Commission has determined that tariffing long distance services could *harm* competition. As discussed in the attached Memorandum, the Commission has expressed concern that tariff requirements might "stifle price competition and marketing innovation,"[6] and could "reduce incentives for competitive price discounting, constrain carriers' ability to make rapid, efficient responses to changes in demand and cost, impose costs on carriers that attempt to make new offerings, and prevent customers from seeking out or obtaining service arrangements specifically tailored to their needs."[7] The Commission also expressed concern that tariffing long distance services could "facilitate tacit coordination of prices" among carriers. And the extensive cost support required in the tariffing process might "discourage the introduction of innovative new service offerings, because it requires a carrier to reveal its financial information to its competitors."[8]

In addition, as noted above, the Commission has concluded that structural separation imposes additional costs and inefficiencies with no corresponding consumer benefit, and has determined that structural separation prevents carriers from taking advantage of scope economies

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[6] *Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area and Policy and Rules Concerning the Interstate Interexchange Marketplace,* 12 FCC Rcd 15756, ¶ 88 (1997).

[7] *Id.* ¶¶ 89-90.

[8] *Id.*

that the carriers could use to produce different services,[9] and inhibits carriers from providing new services.[10] And as the attached Memorandum shows, the CEI and ONA rules likewise add costs and force Verizon to operate in an inefficient manner. As a result, not only is enforcing these regulations not necessary to protect consumers; since enforcing them would affirmatively harm competition, enforcing the regulations would undermine the benefits of competition that consumers now enjoy.

As for the third requirement, in determining whether forbearance is "in the public interest," the Commission must again consider whether forbearance will promote competitive market conditions and benefit consumers. The same benefits to competition and to consumers discussed above ensure that forbearance is in the public interest. *See* 47 U.S.C. § 160(b). Consumers in all parts of the country will benefit from removing outmoded and artificial regulatory handicaps from Verizon's interexchange services. Conversely, application of tariffing requirements, price cap rules, *Computer III*, and structural separation requirements specified here would *harm* the public interest by undermining the robust competition that exists for long distance services. For confirmation of this principle, one need look no further than the Commission's own *Computer II* decision, which recognized that "the very presence of Title II requirements inhibits a truly competitive, consumer responsive market."[11] This is all the more true when only one competitor in the market is subject to the requirements. Moreover, as the

[9] *See, e.g., Amendment of Section 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry)*, 2 FCC Rcd 3035, ¶ 25 (1987).

[10] *See, e.g., Computer III Remand Proceedings; Bell Operating Company Safeguards and Tier I Local Exchange Company Safeguards*, 6 FCC Rcd 7571, ¶ 8 (1991).

[11] *Amendment of Section 64.702 of the Commission's Rules and Regulations (Second Computer Inquiry)*, 77 F.C.C. 2d 384, ¶ 109 (1980) ("*Computer II*"); *see also Memorandum* pp. 25-27 (noting previous Commission findings that imposition of tariffs in a competitive environment affirmatively harms competition).

attached Memorandum makes clear, regulation adds costs to the provision of long distance services, and the Commission has found that the avoidance of unnecessary cost is also in the public interest.[12] This is especially true where, as here, the Commission has not yet concluded its consideration of the appropriate regulatory framework for the integrated provision of long distance services post-272 sunset and has made no finding that the regulations in question would serve any purpose with respect to those services.

Accordingly, the Commission should forbear from enforcing, on an interim basis, the specific requirements set forth above.[13]

Respectfully submitted,

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February 28, 2006

[12] *See Computer II*, ¶ 109.

[13] Rules 53.101 through 53.213 will no longer apply as a matter of law after sunset of section 272. These rules implement section 272(b), (c), (d), and (g) of the 1996 Act, which are the provisions of section 272 that sunset automatically. 47 U.S.C. § 272(f). There would be no legal basis for continuing to enforce such rules after the statutory provisions they implement no longer have legal effect.

THE VERIZON TELEPHONE COMPANIES

For the purposes of this filing, the Verizon companies participating in this filing are the following companies affiliated with Verizon Communications Inc.:

Verizon local exchange carriers:

Contel of the South, Inc. d/b/a Verizon Mid-States
GTE Southwest Incorporated d/b/a Verizon Southwest
Verizon California Inc.
Verizon Delaware Inc.
Verizon Florida Inc.
Verizon Maryland Inc.
Verizon New England Inc.
Verizon New Jersey Inc.
Verizon New York Inc.
Verizon North Inc.
Verizon Northwest Inc.
Verizon Pennsylvania Inc.
Verizon South Inc.
Verizon Virginia Inc.
Verizon Washington, DC Inc.
Verizon West Coast Inc.
Verizon West Virginia Inc.

Verizon long distance companies:

Bell Atlantic Communications, Inc. d/b/a Verizon Long Distance
NYNEX Long Distance Company d/b/a Verizon Enterprise Solutions
Verizon Select Services Inc.
Verizon Global Networks Inc.

Verizon Business companies providing domestic local and long distance service:

MCI Communications Services, Inc.
MCImetro Access Transmission Services LLC
MCImetro Access Transmission Services of Massachusetts, Inc.
MCImetro Access Transmission Services of Virginia, Inc.

On Jan. 6, 2006, MCI, Inc. merged into MCI, LLC, a wholly owned subsidiary of Verizon Communications Inc. Those MCI business units and certain other Verizon business units that serve enterprise and government customers now call themselves Verizon Business; those MCI business units serving consumer residential and small business customers continue to operate using the name MCI.

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MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF VERIZON'S PETITIONS FOR INTERIM WAIVER OR FORBEARANCE

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MEMORANDUM OF
POINTS AND AUTHORITIES
IN SUPPORT OF VERIZON'S PETITIONS
FOR INTERIM WAIVER OR FORBEARANCE

The competitive landscape is very different from the last time the Commission looked at rules relating to provision of long distance service by affiliates of incumbent local exchange companies. Competition for all kinds of telephone services, including long distance services, is robust and vigorous. Where end users once bought local service from their local phone company and long distance service from one of a number of interexchange carriers, they now can choose among a variety of all distance services offered by a wide range of intermodal providers. Cable companies, wireless carriers, and VoIP providers all offer services that compete with traditional wireline telephony and long distance services.

In light of the extensive competition for long distance service, applying outmoded regulations is unnecessary and contrary to the public interest. The Commission has long recognized that competition is the best form of "regulation." Consumers in all parts of the country will benefit from removing outmoded and artificial regulatory handicaps from the BOCs and incumbent independent LECs. Conversely, imposing tariffing, price cap, *Computer III*, and accounting regulations on BOCs' long distance services but not on other competitors, will harm the public interest. Similarly, imposing structural separation requirements on incumbent independent LECs that are not imposed on other competitors also harms the public interest.

Verizon has obtained authority to provide in-region, interLATA services in each of the former Bell Atlantic jurisdictions pursuant to section 271 of the 1996 Act. With such authorization, section 272 required Verizon to provide long distance services through a fully separate affiliate for three years. Certain section 272 safeguards continue beyond this three-year period. 47 U.S.C. § 272(e). The section 272 structural and related requirements will sunset for Verizon in its last group of former Bell Atlantic states on March 19, 2006. Verizon also includes the former GTE service territories. The former GTE companies are subject to structural separation requirements applicable to independent ILECs. 47 C.F.R. § 64.1903(a)(1), (2), (3). The structural separation requirements for the former GTE service areas will not sunset.

As Verizon makes plans for the most efficient way to operate post-272 sunset, it is faced, in the former Bell Atlantic service areas, with the choice of continuing to offer long distance services through affiliates that meet all of the section 272 requirements, or potentially becoming subject to dominant carrier regulations. Neither of these policy choices makes economic sense. In the former GTE service areas, Verizon does not even have this choice, but will continue to be subject to structural separation requirements even as the more rigorous section 272 requirements sunset. These requirements impose significant costs on Verizon's customers. For example, as described in more detail below, as Verizon moves toward greater use of broadband to serve its customers, these regulations may impose design limitations for IP-based and high speed services, which result in unnecessarily costly and complex networks. The complexity and unnecessary interconnections that must be incorporated to comply with section 272 diminish the quality of the services that can be provided and make the services less reliable than they would be if they could be designed more efficiently and without these regulatory impositions.

Although the Commission has initiated proceedings to investigate the appropriate classification of BOC long distance services post-272 sunset,[1] its orders to date imply that its dominant carrier regulations could apply.[2] Similarly, the Commission is considering the appropriate classification of incumbent independent LEC long distance services.[3]

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[1] *Section 272(f)(1) Sunset of the BOC Separate Affiliate and Related Requirements,* Notice of Proposed Rulemaking, 17 FCC Rcd 9916 (2002); *Section 272(f)(1) Sunset of the BOC Separate Affiliate and Related Requirements*, Further Notice of Proposed Rulemaking, 18 FCC Rcd 10914 (2003) ("*272 Sunset FNPRM*").

[2] *Section 272(f)(1) Sunset of the BOC Separate Affiliate and Related Requirements*, 17 FCC Rcd 26869, n.8 (2002) ("Verizon will be deemed nondominant in the provision of in-region interLATA, domestic, interstate service only insofar as that service is provided through an affiliate that complies with section 272 and our implementing rules"); *272 Sunset FNPRM*, ¶ 5 (Commission "decision to accord non-dominant treatment to the BOC interLATA affiliates' provision of interexchange services was predicated on the presence of a section 272 separate affiliate and full compliance with the structural, transactional, and nondiscrimination requirements of section 272 and the Commission's implementing rules").

[3] *272 Sunset FNPRM* ¶ 15.

Accordingly, Verizon requests that the Commission waive or forbear from certain aspects of dominant carrier regulation that would otherwise apply to Verizon if it chooses to offer long distance services in the former Bell Atlantic service areas other than through a 272-compliant subsidiary after March 19, 2006. In particular, Verizon requests a limited waiver of or, in the alternative, forbearance from section 203 of the Communications Act and from the dominant carrier tariffing requirements set forth in Part 61 of the Commission's rules (e.g., 47 C.F.R. §§ 61.28, 61.32, 61.33, 61.38, 61.58, and 61.59) or any such rules that could be read to impose a tariff filing obligation on interstate interexchange or international services; and from price cap regulation on the retail interexchange offerings of Bell companies set forth in Part 61 of the Commission's rules (e.g., 47 C.F.R. §§ 61.41-61.49).[4] In addition, Verizon requests a waiver of, or forbearance from, the Commission's accounting requirements to the extent that they require nonregulated treatment of interexchange services if Verizon decides to provide them through the ILECs after the sunset of section 272; however, accounting for such services that continue to be provided through a separate affiliate should continue to be subject only to GAAP accounting requirements and not otherwise be subject to the Uniform System of Accounts set forth in Part 32 of the Commission's rules.[5] Verizon

[4] Verizon's request for waiver of, or forbearance from, the tariffing, price regulation, CEI/ONA, and Part 63 rules extends only to the provision and offering of long distance services and does not include access services.

[5] Verizon requests a waiver of, or forbearance from, the applicability of *Implementation of the Telecommunications Act of 1996: Accounting Safeguards Under the Telecommunications Act of 1996*, 11 FCC Rcd 17539 (1996) ("*Accounting Safeguards Order*") to the extent this order would require integrated interLATA services offered after the sunset of section 272 to be treated as nonregulated for accounting purposes. The requested waiver of or forbearance from the Commission's accounting rules would apply to all interLATA services provided by Verizon on an integrated basis if the Commission grants Verizon's petition.

also requests waiver of or forbearance from the *Computer III* requirements, including Comparably Efficient Interconnection ("CEI") and Open Network Architecture ("ONA") requirements for its interexchange services[6] and from dominant carrier requirements under Part 63 of the Commission's rules concerning the processes for acquiring lines, discontinuing services, assignments or transfers of control, and acquiring affiliations (47 C.F.R. §§ 63.03, 63.12(b)(2), 63.19(b), 63.21(c), and 63.71(c) (second half of the subsection)). Finally, Verizon requests that the Commission waive, or forbear from applying, certain regulations that require incumbent independent LECs providing in-region, interstate, interexchange or international services to provide such services through a separate affiliate that must maintain separate books of account and is prohibited from jointly owning transmission or switching facilities with the local exchange company (47 C.F.R. §§ 64.1901-64.1903).

I. There is extensive and vigorous competition for both local and long distance services offered by BOCs and incumbent independent LECs.

Over the last decade, the telecommunications market has undergone a fundamental revolution. Where end users once bought local service from their local phone company and long distance service from one of a number of interexchange carriers, they now can choose among a variety of all distance services offered by a wide

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[6] *See Amendment of Section 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry)*, 104 FCC 2d 958, ¶¶ 127-31 (1986); *Application of ONA and Nondiscrimination Safeguards to GTE Corporation,* 9 FCC Rcd 4922 (1994). CEI and ONA requirements do not apply to services provided by non-dominant interexchange carriers. *See Computer III Further Remand Proceedings: Bell Operating Company Provision of Enhanced Services; 1998 Biennial Regulatory Review -- Review of Computer III and ONA Safeguards and Requirements*, 14 FCC Rcd 4289 (1999) (noting that CEI and ONA requirements are not applicable to AT&T). Verizon's request here applies only to its interexchange services and not to intraLATA services provided by Verizon ILECs.

range of intermodal providers. Because consumers increasingly view wireless, cable telephony, and VoIP as viable alternatives to wireline service, wireline access lines are now falling at approximately 5 percent annually, and analysts have recognized that Verizon's region is attracting even greater levels of competition than the country as a whole.[7] Industry experts forecast that cable and VoIP will have more than 9 million subscribers by year end and that in five years 45 percent of U.S. households will either be wireless only or will use VoIP to make their calls.[8]

A. Cable

Cable companies began providing mass market voice telephone service over their networks using circuit switches and are now aggressively rolling out VoIP service to their customers in almost all their service territories. By the end of 2003, cable companies offered circuit-switched voice telephone service to more than 15 percent of homes nationwide; by the end of 2004, they offered telephony services (VoIP or switched) to at least 32 percent of U.S. households. The figure is expected to increase to 94 percent by the end of 2007.[9] Some major cable operators, including Time Warner Cable and

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[7] *See* Viktor Shvets, *et al.*, Deutsche Bank, *2006 Preview: Out with the Old, In with the New* at 9 (Dec. 19, 2005) ("In 2005, Verizon continued to suffer the highest rate of loss (ending the year at an estimated rate of around 6.7%). We continue to believe that this is primarily caused by its 'cutting edge' exposure to aggressive cable telephony deployments by CVC and Time Warner"); Jason Armstrong, *et al.*, Goldman Sachs, *Preview in Pictures (PiP) – 4Q2005, Americas Telecom Services* at 2 (Jan. 2006) ("Access line continues to worsen, on average 40 bp worse than last quarter, we estimate. We expect 6.8% line loss from VZ, 130 bp worse than any other RBOC.").

[8] *See* Jeffrey Halpern, *et al.*, Bernstein Research Call, *Quarterly VoIP Monitor: VoIP Gathering Momentum, Expecting 20M Cable VoIP Subs by 2010* at Exhibit 8 (Jan. 17, 2006); Frank G. Louthan, IV, Raymond James & Associates, Inc., *Reassessing the Impact of Access on Wireline Carriers* at 2 (July 11, 2005).

[9] Jeffrey Halpern, *et al.*, Bernstein Research Call, *Quarterly VoIP Monitor: VoIP Gathering Momentum, Expecting 20M Cable VoIP Subs by 2010* at Exhibit 7 (Jan. 17, 2006).

Cablevision, already offer telephony services in all of their footprint, while others, such as Cox, plan to reach that milestone by year-end 2006 at the latest.[10] As one Wall Street analyst has noted: "By the end of 2006, [VoIP] will be offered almost ubiquitously by cable operators."[11]

As a result, there has been rapid growth in the number of cable telephony subscribers. According to FCC survey data, as of January 2004, approximately 13 percent of customers that were offered cable telephony were subscribing to the service.[12] Some cable operators report that, in some areas, their telephony services have been purchased by as much as 20-40 percent of their cable subscribers.[13] Collectively, cable companies are expected to serve more than nine million lines by the end of 2006 and

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[10] *See* Craig Moffett, *et al.*, Bernstein Research Call, *Cable and Telecom: VoIP Deployment and Share Gains Accelerating; Will Re-Shape Competitive Landscape in 2005*, (Dec. 7, 2004); *see also*, Thomson StreetEvents, *TWX – Q4 2004 Time Warner Inc. Earnings Conference Call*, Conference Call Transcript (Feb. 4, 2005) (statement of Time Warner Inc. CFO Wayne Pace); Cablevision News Release, *Cablevision Systems Corporation Reports First Quarter 2005 Results* (May 5, 2005), *available at* http://www.findarticles.com/p/articles/mi_m0EIN/is_2005_May_5/ai_n13672660; *see also* Comcast, presentation at the Bear Stearns 18th Annual Media, Entertainment & Information Conference at 10-11 (Mar. 2, 2005).

[11] Craig Moffett, *et al.*, Bernstein Research Weekly Notes, *Cable and Telecom: VoIP Will Reshape Competitive Landscape in 2005* (Dec. 17, 2004).

[12] *See* Report on Cable Industry Prices, *Implementation of Section 3 of the Cable Television Consumer Protection and Competition Act of 1992*, 20 FCC Rcd 2718, ¶ 37 & Table 10 (2005).

[13] *See, e.g.*, Chris Bowick, SVP Engineering & CTO, Cox Communications, *Cox Communications: Distribution at Its Best*, presentation at the Bear Stearns 17th Annual Media, Entertainment & Information Conference at 19 (Mar. 8, 2004); *Q1 2004 Cox Communications Inc. Earnings Conference Call – Final*, FD (Fair Disclosure) Wire, Transcript 042904as.714 (Apr. 29, 2004) (Pat Esser, Cox executive vice president & COO); Cox Communications, *News Releases: Cox Brings Telephone to Five New Markets in '05* (Mar. 8, 2005) ("In some communities, such as Omaha, Neb. and Orange County, Calif., 40 percent of consumers subscribe to Cox Digital Telephone"), *available at* http://phx.corporate-ir.net/phoenix.zhtml?c=76341&p=irol-newsArticle&t=Regular&id=683077&.

more than 13 million by year-end 2007.[14] Analysts expect that cable companies will achieve an overall penetration rate of 15-20 percent within the next five years.[15]

For example, each of the four largest cable companies in Verizon's footprint has made substantial inroads in providing telephony service:

- *Time Warner*: Time Warner now offers VoIP in all 31 of its markets, passing a total of more than 19 million homes.[16] Time Warner, which claims to be "the 10th largest phone company in America," serves more than 1.1 million subscribers, and is adding an average of more than 19,000 net new subscribers per week.[17] For example, in Portland, Maine at least 19 percent of homes passed are subscribing to Time Warner's VoIP service.[18]

- *Cablevision*: Cablevision now offers telephony service to all of the homes it passes and is already providing service to more than 16 percent of those homes.[19]

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[14] *See* Jeffrey Halpern, *et al.*, Bernstein Research Call, *Quarterly VoIP Monitor: VoIP Gathering Momentum, Expecting 20M Cable VoIP Subs by 2010* at Exhibit 8 (Jan. 17, 2006).

[15] *See, e.g.*, Douglas S. Shapiro, *et al.*, Banc of America Securities Research Brief, *Battle for the Bundle: Mapping the Battlefield, Our First Report from the Front*, at 3 (June 14, 2005) ("Cable should have 19.8 million telephony subs by 2010, or 18% penetration of homes passed"); *see also* Frank G. Louthan IV & Ben Gordon, Raymond James Equity Research, *Reassessing the Impact of Access Lines on Wireline Carriers*, at 1 (July 11, 2005) (estimating that cable and standalone VoIP will reach over 20 percent of residential households by 2010); Jeffrey Halpern, *et al.*, Bernstein Research Call, *Quarterly VoIP Monitor: VoIP Gathering Momentum, Expecting 20M Cable VoIP Subs by 2010* at Exhibit 8 (Jan. 17, 2006) ("we expect all the Bells to see roughly the same level of line losses, approximately 20-22% by 2010"); *See* Frank Governali, *et al.*, Goldman Sachs, *Americas: Telecom Services* (Jan. 12, 2005).

[16] *See* Thomson StreetEvents, *TWX—Q4 2004 Time Warner Inc. Earnings Conference Call*, Conference Call Transcript (Feb. 4, 2005) (statement of Time Warner Inc. CFO Wayne Pace); Time Warner Cable, *About Us Company Highlights*, *available at* http://www.timewarnercable.com/corporate/aboutus/companyhighlights.html.

[17] *Time Warner Inc. at Credit Suisse First Boston Media Week – Final*, FD (Fair Disclosure) Wire, Transcript 120805ae.718 (Dec. 8, 2005) (Time Warner Inc. chairman and CEO Dick Parsons); Time Warner Press Release, *Time Warner Inc. Reports Results for 2005 Full Year and Fourth Quarter* (Feb. 1, 2006).

[18] *See* T. Horan, *et al.*, CIBC World Markets, *Cable-Telco Duopoly Under Pressure* at 9 (Sept. 25, 2005).

[19] Cablevision Systems News Release, *Cablevision Systems Corporation Reports Fourth Quarter and Full Year 2005 Results* (Feb. 27, 2006). *See also* Jeffrey Halpern, *et*

Analysts expect that Cablevision's penetration rate will exceed 21 percent by the end of the year.[20] Cablevision added an average of approximately 10,000 customers per week in the fourth quarter of 2005 and now serves more than 731,000 customers.[21] Cablevision reported that it is "growing at a rate of approximately 1% of [its] homes passed per month."[22]

- *Comcast*: Comcast recently announced that it already has over 16.5 million homes marketable with its Digital Voice and circuit-switched offerings, or 40 percent of its footprint nationwide.[23] Comcast plans to market its voice service to 80 percent of its footprint by the end of 2006.[24] Comcast is currently providing service to more than 1.3 million customers, and is adding more than 14,000 customers per week.[25] The company expects to add one million VoIP customers this year and to achieve 20 percent penetration within five years.[26]

- *Cox*: Cox offers circuit-switched voice telephone service and VoIP to approximately 75 percent of the 10 million homes it passes nationally, covering

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al., Bernstein Research Call, *Quarterly VoIP Monitor: VoIP Gathering Momentum, Expecting 20M Cable VoIP Subs by 2010* at Exhibits 7-8 (Jan. 17, 2006) (estimating 16 percent penetration as of year-end 2005).

[20] Jeffrey Halpern, *et al.*, Bernstein Research Call, *Quarterly VoIP Monitor: VoIP Gathering Momentum, Expecting 20M Cable VoIP Subs by 2010* at Exhibits 7-8 (Jan. 17, 2006).

[21] Cablevision Systems News Release, *Cablevision Systems Corporation Reports Fourth Quarter and Full Year 2005 Results* (Feb. 27, 2006).

[22] *Q2 2005 Cablevision Systems Corp. Earnings Conference Call - Final*, Transcript 080905ag.778, FD (Fair Disclosure) Wire (Aug. 9, 2005).

[23] Comcast Press Release, *Comcast Reports Third Quarter 2005 Results* (Nov. 3, 2005); Comcast, Presentation at the Citigroup 16th Annual Entertainment, Media and Telecommunications Conference (Jan. 9, 2006).

[24] Thomson StreetEvents, *CMCSA – Q4 2005 Comcast Corporation Earnings Conference Call* at 5 (Feb. 2, 2006).

[25] *Id.*

[26] *Id.*; Thomson StreetEvents, *CMCSA – Q4 2004 Comcast Corporation Earnings Conference Call, Final Transcript* (Feb. 3, 2005) (Comcast COO & President Steve Burke: "[W]hen you look at what Cox, and more recently Cablevision, and others have done in this business, we think the 20 percent penetration is very reasonable within a five-year time period").

22 of its major markets.[27] Cox serves more than 1.5 million telephone customers nationwide.[28]

Moreover, cable modem service has a significant lead over DSL in broadband subscribership.[29] As a result, cable operators will be able to take advantage of their lead in video and data to grow telephony.

B. Wireless

Wireless voice service is a close alternative for wireline service, is priced similarly, and thus competitively disciplines wireline services. As a result, wireless companies continue to increase their minutes of use and subscriptions at a double-digit pace, while wireline services are experiencing declines in number of access lines and minutes.

Along with cable, wireless service currently provides a significant alternative to traditional telephony.[30] A number of national wireless providers including Verizon Wireless, Cingular, Sprint Nextel, and T-Mobile, along with significant regional competitors, compete with landline service. As the FCC noted, wireless service has

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[27] Cox News Release, *Cox Digital Telephone Goes Live in Las Vegas* (Nov. 28, 2005).

[28] Cox News Release, *Cox Communications Announces Second Quarter and Year-to-Date Financial Results for 2005* (Aug. 9, 2005).

[29] *See, e.g.*, Viktor Shvets, *et al.*, Deutsche Bank, *4Q05 Preview: Reasonable Quarter, Bolstered by Wireless and Data* at Figure 9 (Jan. 18, 2006) (estimating cable's share of broadband subscribers at 57 percent as of year-end 2005); Jonathan Chaplin, *et al.*, JP Morgan, *State of the Industry: Consumer* at Table 35 (Jan. 13, 2006) (estimating cable's share of broadband subscribers at 54 percent as of year-end 2005); Ido Cohen, *et al.*, Credit Suisse, *2006: Mix Is the Key* at Exhibit 3 (Jan. 24, 2006) (estimating cable's share of broadband subscribers at 57 percent as of year-end 2005).

[30] *See* David W. Barden, et al., Banc of America Securities, *Setting the Bar: Establishing a Baseline for Bell Consumer Market Share* at 5 (June 14, 2005).

grown so spectacularly that of 362 million voice lines counted by the FCC at the end of 2004, 181.1 million – more than 50 percent – are wireless.[31]

Both consumers and suppliers[32] view wireless as an alternative to wireline services, resulting in wireless putting competitive pressure on wireline. Wireless displacement occurs on at least three levels. First, wireless minutes generally displace wireline minutes. Second, because of the prevalence of wireless phones, customers buy fewer second or third lines than they would absent competition from wireless. Third, an increasing number of customers use wireless as their primary service or use only wireless minutes by "cutting the cord."

Consumer surveys reveal that wireless service has displaced 64 percent of long distance and 42 percent of local calling from landlines in households with wireless

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[31] *See Federal Communications Commission Release Data on Local Telephone Competition* (rel. July 8, 2005), *available at* http://www.fcc.gov/Bureaus/Common_Carrier/Reports/FCC-State_Link/IAD/lcom0705.pdf.

[32] *See Applications of Nextel Communications, Inc. and Sprint Corp. for Transfer of Control*, WT Docket No. 05-63, at 30, 31 (filed Feb. 8, 2005) (the combined Sprint/Nextel "will position its services as a competitive alternative to wireline service, to the benefit of intermodal competition and consumers," and "will have a greater ability to compete for business that historically has gone to wireline companies"); *see also* AT&T Corp., Form 10-K (Mar. 15, 2004) ("Consumer long distance voice usage is declining as a result of substitution to wireless services, internet access and email/instant messaging services, particularly in the 'dial one' long distance, care and operator services segments") *available at* http://www.sec.gov/Archives/edgar/data/5907 /000095012304003304/y92576e10vk.txt; *see also* MCI, Inc., Form 10-K (Apr. 29, 2004) ("[W]ireless telephone companies . . . have increased their network coverage, improved service quality, started to provide bundled wireless products and lowered prices to end-users. As a result, customers are beginning to substitute wireless services for basic wireline service causing these companies to gain market share from providers of wireline voice communications"), *available at* http://www.sec.gov/Archives/edgar/data/723527 /000119312504074088/d10k.htm; *Petition to Deny of Qwest Communications Int'l, Inc.*, WC Docket No. 05-65 at 35 (filed Apr. 25, 2005) ("Consumers have demonstrated that they are increasingly willing to replace our wireline service with the wireless services of our competitors").

phones.[33] A Yankee Group survey found that *approximately 10 percent of wireless users* do not have a landline phone at all.[34] Industry trends and market demographics suggest that this competition will only intensify.[35] Indeed, some Wall Street analysts "look for wireless substitution to be the largest displacer of access lines over the next five years."[36]

The wireless carriers' all-distance plans, beginning in 1999 and 2000, led to massive displacement away from landline long distance calls and reversed what had been a steady increase in wireline long distance minutes. "Thanks to unlimited night and weekend minutes . . . cellphone plans are the method of choice when it comes to long distance calling from home."[37]

The absolute increase in wireless minutes has been explosive. By 2004, wireless minutes of use had risen to 1.1 trillion, an increase of 32.7 percent from 2003 and more

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[33] Kate Griffin, Yankee Group, *Pervasive Substitution Precedes Displacement and Fixed-Mobile Convergence in Latest Wireless Trends* at 5 & Exhibit 3 (Dec. 2005).

[34] *Id.* at 5. *See also* J. Armstrong, *et al.*, Goldman Sachs, *2006 Outlook – Stuck in Neutral* at 31 (Jan. 13, 2006) (wireless-only customers represent a 12.5 percent share of the residential market).

[35] *See, e.g.,* Blake Bath, Lehman Brothers, *Wireless Services: Industry Overview, Raising '06-'08 Wireless Net Adds by 50%,* at 3 (June 16, 2005) (increasing by 50 percent estimates of net wireless subscriber additions through 2008 and predicting that wireline displacement, penetration of the youth market, and expanded wireless data offerings will generate "12-18 million new wireless subscribers per year for the next several years," resulting in 85 percent market penetration by 2010).

[36] F. Louthan, *et al.*, Raymond James, *VZ, SBC, BLS, Q: Cable Threat Comparison for RBOCs* at 2 (July 11, 2005); V. Shvets, *et al.*, Deutsche Bank, *The Hotline: 1Q05 Wireline Post-Mortem* at p. 4 (May 9, 2005) ("wireless remains the single biggest killer of both total and retail access lines" and "the rate of wireless cannibalization has accelerated in the last four quarters . . . . Although not all numbers are in yet, it is likely that close to [one million] access lines were lost to wireless [in the first quarter of 2005], maintaining the ratio of around 50% of 'kills'").

[37] W. Mossberg, *The Mossberg Solution: Turning Your Home Phone into A Cellphone – Call-Forwarding Devices Let You Use Cellular Service on a Traditional Phone*, WALL ST. J., Dec. 3, 2003 at D6.

than 300 percent since 2000.[38] *This increased usage has been accompanied by a rapid* erosion in traditional distinctions between the locations from which subscribers use fixed and mobile service, as subscribers increasingly use their mobile devices at stationary locations from which wireline alternatives would readily be used. For example, a Yankee Group survey found that the percentage of wireless usage in the home by mobile phone users grew from 11.6 percent to 24.1 percent of total usage between 2001 and 2005.[39] The percentages do not fully convey the magnitude of the actual growth in the use of wireless in the home. When applied to the total minutes of wireless use, these percentages mean that wireless minutes consumed at home soared from approximately 28 billion in 2001 to approximately 297 billion in 2004.[40] As the report notes, the actual growth in minutes that displace home calling may be much greater, because many wireless users make calls from their cars that they otherwise would have made at home.[41]

During the same period that wireless minutes have grown rapidly, wireline minutes have declined. The FCC's own data show that average residential wireline toll minutes have declined rapidly for the industry as a whole – from an average of 149 minutes per month in 1997, down to only 71 minutes per month in 2003 (and

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[38] *See* CTIA-The Wireless Association, Background on CTIA' s Semi-Annual Wireless Industry Survey, *Reported Wireless Minutes of Use Exceed One Trillion in 2004* at 8 (2005), *available at* http://files.ctia.org/pdf/CTIAYearend2004Survey.pdf ("CTIA Semi-Annual Survey"); *see also* Federal Communications Commission, *9th Annual CMRS Competition Report*, (rel. September 28, 2004) *available at* http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-04-216A1.pdf.

[39] Keith Mallinson, Yankee Group, *Wireless Substitution of Wireline Increases Choice and Competition in Voice Services*, at 5 (July 27, 2005). During the same time period, wireless usage in the office grew from 5.5 percent to 9.7 percent of total usage. *Id.*

[40] *Id.* at 1, 5. The minutes of usage at home figure for 2004 is calculated by applying the 2005 usage at home percentage to total wireless minutes for 2004.

[41] *Id.* at 5.

undoubtedly much less today, given the increase in wireless and decrease in wirelines).[42] In total, consumers reduced the number of long distance minutes of use on landline phones by 52 percent between 1997 and 2003.[43] Moreover, approximately 32.9 percent of wireless subscribers use their landline only for local calls.[44] These findings "suggest[] that wireless is eroding the usage of wireline long distance and local toll services twice as much as the rate of complete wireless substitution."[45] Not surprisingly in light of these trends, data from the Telecom Industry Association reveal that revenue from wireless services has outpaced revenue from wireline long distance since 2003 and will surpass revenue from landline local exchange calls by 2007.[46]

Another manifestation of wireless competition is that a growing share of wireless subscribers are abandoning their wireline phones altogether – "cutting the cord." Lehman Brothers estimates that 16 million wireline access lines have been lost to wireless since 1999, and that wireless substitution will continue to add more than 6 million new wireless subscribers each year.[47] As a result, analysts predict that the

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[42] *See* Ind. Anal. & Tech. Div., Wireline Competition Bureau, *Trends in Telephone Service* at Table 14.2 (June 2005) (includes: IntraLATA-Intrastate, InterLATA-Intrastate, IntraLATA-Interstate, InterLATA-Interstate, International, Others (toll-free minutes billed to residential customers, 900 minutes, and minutes for calls that could not be classified)).

[43] *See id.*

[44] David Chamberlain, In-Stat/MDR, *Cutting the Cord: Consumer Profiles and Carrier Strategies for Wireless Substitution* at 1 (Oct. 2005).

[45] David Chamberlain, In-Stat/MDR, *Cutting the Cord: Consumer Profiles and Carrier Strategies for Wireless Substitution* at 6 (Oct. 2005).

[46] *See TIA*, Total Telecom, *U.S. Telecoms Services Revenue to Rise 3.6% in 2005* (Mar. 4, 2005) (citing TIA's 2005 Market Review and Forecast).

[47] B. Bath, Lehman Brothers, *Telecom Services - Wireline* at Figure 11 (July 7, 2005). *See also* T. Horan, *et al.*, CIBC World Markets, *3Q05 Communications and Cable Services Review* at Exhibit 12 (Nov. 23, 2005) (estimating wireless substitution at